United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

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To be argued by
TERENCE H. BENBOW

74-1533

United States Court of Appeals
FOR THE SECOND CIRCUIT

In the Matter of

SAPPHIRE STEAMSHIP LINES, INC.,
Bankrupt-Appellant,

and

J. READ SMITH,
Trustee-Appellant,

against

WINTHROP, STIMSON, PUTNAM & ROBERTS, ATTORNEYS FOR E. BERGENDAHL CO., INC. (NEW YORK) AND E. BERGENDAHL CO., INC. (PHILADELPHIA), CREDITORS,
Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

APPELLEES' BRIEF

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APPELLEES' BRIEF

Preliminary Statement

The Trustee has appealed from that portion of the Decision and Order made herein by the Honorable Milton Pollack in *In Re Sapphire Steamship Lines, Inc.*, 373 F. Supp. 727 (1974) (77a),* which rejected the recommendation of Bankruptcy Judge Aza S. Herzog in his Certificate on Allowances (63a) to deny *in toto,* (72a) the application of the law firm of Winthrop, Stimson, Putnam & Roberts ("Winthrop, Stimson") for an allowance of $175,000 in attorneys' fees for services rendered to the Bankrupt Estate and for reimbursement of $3,108.43 in disbursements incurred in connection with those services.

In the second paragraph of his introductory Statement, the Trustee summarizes inaccurately, and much too narrowly, the instructions of the Court in remanding to

* Unless otherwise indicated, numbers in parentheses refer to pages in the Joint Appendix.

the Bankruptcy Court the matter of allowances for attorneys' fees. (Appellant's Brief P.2) Judge Pollack's instructions read:

> ". . . it is preferable that all those equitably entitled to be compensated should be considered at the same time to avoid any individual or overall distortions. [citations]
>
> "Accordingly, the Bankruptcy Judge should, at the same time, reconsider the relative contributions of the Special Attorney and the Regular Attorney for the Trustee and the attorneys for the objecting creditors and such compensation as is fair and reasonable for the services of each in the creation of the fund in Court and as is reasonable overall and in relation to each other should be allowed payable out of the settlement fund." (96a-97a)

The Bankruptcy Judge should, therefore, on remand consider simultaneously the fees to be awarded to Special and Regular Counsel for the Trustee and to Winthrop, Stimson for their services in the creation of the fund.

Issues

This appeal presents two questions:

1. Whether this Court should affirm the finding by Judge Pollack that the services rendered by Winthrop, Stimson contributed to the enormous enhancement of a fund inuring to the benefit of all creditors of the Bankrupt Estate?

We submit that the answer should be in the affirmative.

2. May attorneys through whose non-duplicative services a bankrupt's estate has been greatly enhanced for the benefit of all creditors be compensated for those services although the attorneys were not expressly authorized by the Bankruptcy Court to render those services?

The District Court answered this question in the affirmative.

Summary of Argument

The only important asset of Sapphire Steamship Lines, Inc., the bankrupt, was a pending action against certain shipping companies for damages sustained as a result of actions alleged to be in violation of Federal Antitrust Laws and Sec. 810 of the Merchant Marine Act of 1936. Winthrop, Stimson and the Assistant U.S. Attorney opposed an offer of $1,600,000 in settlement over the strong resistance of the Trustee and his counsel, with the result that the case was finally settled for $2,473,070.

The Trustee herein interposed no objection before the Bankruptcy Judge to Winthrop, Stimson's application for the allowance of an attorney's fee for their services. Moreover, when the Trustee submitted argument before the District Court in support of the Bankruptcy Judge's recommendation to deny Winthrop, Stimson's application, his argument was addressed solely to the legal question whether the District Court had the power to grant a fee in the absence of express court authorization to perform the services which formed the basis for the application. In his brief herein the Trustee proffers for the first time the factual argument that the 1,769 hours of time expended by Winthrop, Stimson in connection with this matter (52a) were in no way "responsible for the creation of a fund from which other creditors benefited" (App. Brief p. 5)*. We submit that, having failed to raise this factual question before either the Bankruptcy Judge or the District Court, the Trustee is precluded from doing so at this time.

Assuming, however, *arguendo*, that this Court concludes that, notwithstanding the Trustee's failure to raise the question below, the question is nonetheless properly be-

* It should be noted that the creditors themselves felt otherwise as is evidenced by the fact that not a single creditor has ever voiced objection to Winthrop, Stimson's application, and, in fact, most of the major creditors herein have made filings both before the Bankruptcy Judge and the District Court in support of our application (101a-125a).

fore it, the factual question presented should not be decided *de novo* herein but, rather, should be reviewed by this Court's application of the "clearly erroneous" standard to the findings of fact made by the District Court, under Rule 52(a) of the Federal Rules of Civil Procedure which provides in relevant part that "findings of fact shall not be set aside unless clearly erroneous, ..." We submit that based on the entire record, the findings of the District Court were not clearly erroneous but, on the contrary, Judge Pollack was clearly correct in finding that "[f]rom the time of their opposition to the 1970 offer of compromise and throughout the proceedings in the following years the firm of Winthrop, Stimson, Putnam & Roberts undisputably rendered services inuring to the benefit of the creditors of the Bankruptcy Estate as a class and which contributed to the enormous enhancement of the Estate that was achieved." (88a) (Point I *infra*)

Contrary to the assertion of the Trustee in his Point II, that Judge Pollack's decision "is inconsistent with decisions of this Court denying compensation to a volunteer even for beneficial services," (App. Brief p. 8), a reading of the applicable case law makes manifest that this Court has held consistently that it is within the powers of the Bankruptcy Court, in appropriate circumstances, to make such awards for attorney's fees as justice and equity might dictate. Moreover, the most widely recognized factual situation considered appropriate by courts invoking such equitable powers is where an attorney has protected or created a fund in which others may share—precisely the factual situation at bar.

The Trustee argues, however, that in any event an award to Winthrop, Stimson cannot be sustained because of our failure to obtain prior court approval to perform such services on behalf of the Bankrupt Estate. We submit that this Court's previous decisions, in light of the unique circumstances herein, must give rise to a contrary conclusion.

Generally, the Trustee is acting in the best interests of the Bankrupt Estate. Accordingly, in the name of good administration, prior court approval must normally be obtained if services performed on behalf of the Bankrupt Estate are to be compensated from that Estate. This Court, however, has expressly engrafted an exception on that general rule by omitting the requirement of prior court approval where:

> (1) the individual seeking compensation has not rendered services duplicating the efforts of others, and
>
> (2) it was reasonable to conclude that the Trustee would not have performed such services.

In the instant case, services performed by Winthrop, Stimson were not duplicative of anyone else's efforts and, as a review of the facts will demonstrate, it is reasonable to conclude that the Trustee and those acting on his behalf would not and did not perform the services rendered by our firm on behalf of the Bankrupt Estate. Accordingly, the exception rather than the general rule is clearly applicable to the instant case. (Point II *infra*)

ARGUMENT

POINT I

The Record Herein Supports The District Court's Finding That The Services Rendered By Winthrop, Stimson Enormously Enhanced The Settlement Fund, Which Inured To The Benefit Of The Bankrupt Estate As A Whole

The Trustee intersperses throughout his brief bald factual assertions to the effect that the services performed by Winthrop, Stimson in connection with this matter have in no way contributed to the enhancement of the Bankrupt Estate. By such assertions, the Trustee is attempting to raise for the first time in this Court a question of fact which

the Trustee failed to place in issue either before the Bankruptcy Judge or the District Court. We submit that having failed to raise the question below, the Trustee should be precluded from raising it here. *Fortunato* v. *Ford Motor Co.*, 464 F.2d 962, 967 (2d Cir.), *cert. denied*, 409 U.S. 1038 (1972); *First National Bank* v. *Pepper*, 454 F.2d 626, 636 (2d Cir. 1972); *Dubnoff* v. *Goldstein*, 385 F.2d 717, 720 (2d Cir. 1967); *List* v. *Fashion Park, Inc.*, 340 F.2d 457, 461 (2d Cir.), *cert. denied*, 382 U.S. 811, *rehearing denied*, 382 U.S. 933 (1965). Accordingly, the instant appeal should be limited to the sole question of law raised by the Trustee and dealt with in Point II of this brief.

Should the Court conclude otherwise and determine that the question of fact whether the services performed by Winthrop, Stimson have enhanced the Bankrupt Estate is properly before it, the following summary of the services performed by Winthrop, Stimson in connection with this matter (more fully developed at 17a-52a, 8a-9a) adequately establishes that the District Court did not reach a clearly erroneous finding when it concluded that "there is no question but that a tangible benefit has been conferred on the Estate as a whole" by the services rendered by Winthrop, Stimson. (94a)

A. We Opposed the Initial Approval by the Bankruptcy Judge of the $1,600,000 Settlement Offer at the Hearing on September 14, 1970. (17a-19a)

In the summer of 1970 settlement offers in the antitrust case, totalling $1,600,000, were accepted by the Trustee and submitted to the Bankruptcy Judge for approval. Based on our experience in antitrust matters and a limited analysis of the reasons offered by Special Counsel in support of the proposed settlement, we concluded that $1,600,000 was not adequate. We appeared at the hearing on behalf of our clients and opposed the settlement. In his decision dated

September 21, 1970 the Bankruptcy Judge approved the $1,600,000 settlement on the grounds that: (a) no evidence had been introduced to controvert the fact that basic records of the bankrupt were missing, (b) efforts by the Trustee and by Special Counsel to locate these records had been unsuccessful, (c) certain important witnesses were unavailable, and (d) the argument of Special Counsel that he seriously doubted that he could prove damages.

B. We, Acting Jointly with the Assistant U. S. Attorney, Were Successful in Getting the $1,600,000 Settlement Disapproved at a Rehearing on November 30, 1970. (20a-28a)

We investigated the reasons stated by Special Counsel on the difficulty of proving damages, and conferred with Counsel and Special Counsel to the Trustee, with the then Assistant U.S. Attorney, Peter DeFilippi, and with attorneys for other creditors. We interviewed the key witnesses who, it had been stated, were unavailable, and ascertained they were available. We interviewed the chief accounting officer of plaintiff-bankrupt and obtained information and leads on the availability of basic accounting records of Sapphire and on damages. We determined that the basic accounting records of Sapphire could be located and missing records could be reconstructed. We informed the Assistant U.S. Attorney and counsel for other large creditors of the results of our investigation, and decided that a motion for rehearing should be filed. All agreed that better results could be obtained at substantially less expense if the U.S. Attorney's office and the office of Winthrop, Stimson coordinated their efforts. In addition, Mr. DeFilippi stated he was not an expert in antitrust litigation, relied to a great extent on the expertise of Winthrop, Stimson in antitrust litigation, and that the knowledge and experience of Mr. Benbow, a member of Winthrop, Stimson, were invaluable. (119a, 120a) We pre-

pared and filed a joint application for rehearing, together with accompanying exhibits.

The Trustee strenuously opposed the application for rehearing.

As his response Special Counsel submitted an affidavit (25a, 26a) by Maxwell Blecher, Esq., in which he stated, in substance, that (a) he had personally conducted substantially all of the settlement negotiations; (b) he had recommended that the Trustee accept the offer of $1,600,000; (c) he had considered the objections of the creditors to the proposed settlement; (d) he had carefully examined the facts recited in the affidavits in support of their objections and *found nothing which altered his strong conviction that the $1,600,000 settlement offer was favorable and should be accepted.* He concluded his affidavit by stating:

> *"I am certain that if attorneys from their offices familiar with antitrust cases were to devote the time required to make a full study of this case,* as we have done, they, too, would conclude that this is an excellent settlement." (26a)

The application for rehearing was granted by the Referee who, on reargument, vacated his order of September 29, 1970 and thereupon disapproved the $1,600,000 settlement. (We spent 491 hours on this second stage of the proceedings.)

C. The Bankruptcy Judge Granted the Trustee's Motion for Reargument and Affirmed His Disapproval of the $1,600,000 Settlement. (28a-32a)

Thereafter the Trustee moved for reconsideration of the new order, urging again that the $1,600,000 settlement was excellent and the most that could be expected. We made a thorough review of the papers in the proceedings, both those filed in the District Court for the District of Columbia and those theretofore filed in the Bankruptcy Court. We made a further study of financial and accounting records

and other data available. We conferred at length with Mr. DeFilippi, who had just resigned as Assistant U.S. Attorney, and with his successor, Alan B. Morrison. We again submitted jointly a memorandum of law, dated April 16, 1971, in opposition to the application. In his decision dated May 24, 1971 the Bankruptcy Judge granted the Trustee's Motion for Reargument and adhered to his earlier decision disapproving the $1,600,000 compromise. In his decision, the Bankruptcy Judge stated:

> *"The trustee seeks to punch further holes in its own position in the anti-trust case in order to persuade me to authorize the compromise.* These, too, are arguable matters to be determined at the trial of the issues.
>
> * * *
>
> "There is no doubt that bankrupt was forced out of business by the conduct of the defendants in the anti-trust action. *Safir* v. *Gibson,* 417 F.2d 972, 974, 978 (2d Cir. 1969). There seems little doubt that they suffered a substantial loss of revenue, a portion of which, it seems, can be established through competent witnesses. Further losses, on invested and borrowed capital may well be established as a direct result of the conspiracy.
>
> "In view of these factors, a compromise, which after payment of the fee of special trial counsel and bankruptcy administration expenses would leave nothing for general creditors ought not, in the face of strong objection, be approved." (32a). (Emphasis added)

(We spent 152 hours on this third stage of the proceedings.)

D. The Trustee Filed a Petition for Review With the District Court and the Defendants Moved to Intervene, Both of Which We Opposed and Judge Lasker Denied. (32a-35a)

On June 16, 1971, the Trustee filed a Petition for Review with the District Court, alleging in substance that the disapproval of the $1,600,000 compromise was not in the best

interests of the Bankrupt Estate. Special Counsel filed a brief with voluminous exhibits attached. Attorneys for the defendants in the antitrust case moved to intervene and submitted lengthy memoranda and exhibits in support of the Trustee's Petition for Review.

We reviewed all the voluminous papers and exhibits submitted by Petitioners and Intervenors, and made a further study of the facts and law pertaining to the pending antitrust case in the District of Columbia. After conferences with the Assistant U.S. Attorney we prepared and submitted a Joint Memorandum of Facts and Law in Opposition to the Petition for Review.

At the hearing before Judge Lasker both Joseph L. Alioto (Special Counsel) and several counsel for the defendants argued at great length urging approval of the $1,600,000 offer. Winthrop, Stimson and the Assistant U.S. Attorney argued in favor of upholding the Referee's decision disapproving the offer.

Judge Lasker denied the Trustee's Petition for Review and the motions of the defendants to intervene. (35a) (We spent 211 hours on this fourth stage of the proceedings.)

E. During Negotiations in 1972 Winthrop, Stimson and the Assistant U.S. Attorney Attended at Conferences Requested by Defendants and opposed a Tentative Offer of $2,000,000 Agreed to and Recommended by Special Counsel. (36a-44a)

At various times during these proceedings, counsel for "Non-Trade" and for "Trade" defendants requested conferences with the Assistant U.S. Attorney to discuss the offers of settlement aggregating $1,600,000, and to urge the U.S. Attorney to withdraw his opposition on the ground that the priority claims of the United States would be substantially paid if the offer of $1,600,000 was approved. The Assistant U.S. Attorney currently in charge of the matter for the United States desired Mr. Benbow and Mr. Trygstad

or Mr. Berger of Winthrop, Stimson present as Winthrop, Stimson had devoted a substantial amount of time to the investigation and analysis of damages suffered by the Bankrupt, in researching questions of law pertaining to the alleged violations of the Sherman Act and the Merchant Marine Act of 1936, in extensive interviewing of witnesses, and in the preparation of memoranda of facts and law and of exhibits. We discussed the merits of the case with the Assistant U.S. Attorney before these conferences, and participated in the discussions at the conferences.

In March 1972, a conference was called in Washington by defendants' counsel to discuss a "sweetening of the pot." In January 1972 Alan Morrison had resigned as Assistant U.S. Attorney. His successor in charge of this matter, T. Gorman Reilly, Esq., requested we brief him on the background and facts of the case, and our analysis of the questions of law, the liability of defendants and the damages suffered by the Bankrupt. We made available to Mr. Reilly the documents and evidentiary material in our file which we had built up during the prior stages in these proceedings. (38a-39a)

At this conference in Washington counsel for the defendants stated that (a) they were prepared to increase their offer in settlement from $1,600,000 to $2,000,000, (b) Special Counsel had agreed to limit his application for fees to those which he would have claimed if the original offer had been approved by the Referee, and (c) this would leave a net balance which appeared to be sufficient to pay all or substantially all of the government's priority claims against the Bankrupt. (39a-40a)

Mr. Alioto confirmed that he approved and recommended the revised $2,000,000 offer. He stated it was *extremely favorable* to the Bankrupt and should be accepted. The pending litigation was discussed at length. (40a)

The Assistant U.S. Attorney and Winthrop, Stimson informed Counsel for defendants and Special Counsel that

they would oppose acceptance of the new $2,000,000 offer, as they considered the case was strong with respect to proving substantial damages, as well as liability, and the new offer was still substantially inadequate in amount. (41a)

In the fall of 1972, at the request of defendants' counsel, another conference was held in New York City. Defendants' counsel renewed their offer of $2,000,000 and the Assistant U.S. Attorney and Winthrop, Stimson restated their opposition. They stated they would recommend acceptance of an offer in an aggregate sum equivalent to $3,500,000 increased by an amount estimated as attorney's fees, as a reasonable and fair measure of single damages. No agreement was reached and the meeting broke up. (41a-43a)

(We spent 451 hours on this fifth stage of the proceedings.)

F. The Antitrust Case Was Settled in 1973 for $2,473,070, Which We Opposed as Still Grossly Inadequate but Which Was Approved by the Bankruptcy Judge. (44a-51a)

The proceedings in the pending litigation were resumed in the United States District Court in the District of Columbia. Counsel for "Non-Trade" defendants renewed their efforts to settle the claims of Plaintiff-bankrupt against them by again contacting the Assistant U.S. Attorney and offering to increase their first offer of $150,000 to $250,000. Mr. Reilly conferred again with Winthrop, Stimson. After a lengthy review and analysis of the probable liability of the "Non-Trade" defendants, we agreed that the tentative offer of $250,000 was still inadequate. Shortly thereafter counsel for the "Trade" defendants wrote the Assistant U.S. Attorney with a new offer aggregating $2,473,070 (including an increased offer of $300,000 by the "Non-Trade" defendants). They stated they needed to

know whether the Attorney General would recommend acceptance. The new offer was accepted by the Department of Justice and thereupon was presented to the Trustee who accepted it, and settlement papers were drawn.

At the hearing before the Bankruptcy Judge on July 16, 1973 we opposed this new settlement offer as it gave effect only to damages sustained by reason of loss of profits during the period prior to bankruptcy and loss of capital as a result of the bankruptcy of the plaintiff, but did not give effect to loss of future profits. We had reviewed the voluminous material in our files on the question of damages suffered by Plaintiff-bankrupt and obtained and analyzed the recent favorable decision, dated April 9, 1973, by the Maritime Subsidy Board, Docket No. S-243, *Sapphire Steamship Lines, Inc.* v. *AGAFBO*—investigation of alleged Section 810 violation, in which certain of the defendants were found guilty of violating Section 810. We prepared and filed a Memorandum in Opposition to Petition for Approval of Compromise, dated July 12, 1973, together with exhibits, including detailed accounting schedules evidencing the loss of projected future profits from Sapphire's containership program which it was forced to abandon. We opposed the offer as inadequate. In our opinion, based on the evidence available, the probability of a jury reaching a verdict favorable for the plaintiff was excellent if the case were tried (a) on the question of liability of the defendants and (b) on the question of an award of damages substantially exceeding $2,500,000, which under the law would be trebled, plus attorney's fees.

The Bankruptcy Judge approved the settlement of $2,473,070.12. As this enhanced amount would now result in full payment of the priority claims of the United States and payment of an estimated 50% to 75% on all claims of general creditors* we, with the concurrence of attorneys for other creditors, did not take an appeal.

* Claims of creditors have not yet been proved and allowed. This approximation is based on our review and estimate of the allowable claims of creditors.

(We spent 464 hours in this sixth stage of the proceedings.)

Upon the foregoing undisputed factual statement of services rendered by Winthrop, Stimson throughout this proceeding, the District Court concluded:

> "From the time of their opposition to the 1970 offer of compromise and throughout the proceedings in the following years the firm of Winthrop, Stimson Putnam & Roberts undisputably rendered services inuring to the benefit of the Creditors of the Bankrupt Estate as a class and which contributed to the enormous enhancement of the Estate that was achieved.
>
> * * *
>
> "Unquestionably, the services of Winthrop, Stimson, Putnam & Roberts went beyond their representation of the interests of individual creditors. The values ultimately recovered for the Estate over the resistance of the Special Counsel as well as the Trustee and over the initially approved compromise of $1,600,000 went enormously beyond what the Special and general Attorneys for the Trustee had accomplished for the Estate.[2] The government has acknowledged the important association of the Winthrop, Stimson firm in the opposition to the initial settlement and the creation of the new settlement. (88a, 90a-91a)

"2. The record contains a number of affidavits of support for Winthrop, Stimson's fee application from creditors who would equitably bear the burden of any fee awarded to Winthrop, Stimson. There is no opposition to such an award on the record before the Referee, or before this Court."

Rule 52a of the Federal Rules of Civil Procedure provides in relevant part that "findings of fact shall not be set aside unless clearly erroneous, ..." In defining the "clearly erroneous" standard, the Supreme Court has stated:

> "A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 395 (1948).

We submit a review of the record herein demonstrates that no mistake was made by Judge Pollack in finding that the services rendered by Winthrop, Stimson have contributed to the enormous enhancement of the Bankrupt Estate which has inured to the benefit of the creditors as a class.

POINT II

The Services Of Attorneys Which Have Greatly Enhanced The Bankrupt Estate May, In Appropriate Circumstances, Be Compensated From That Estate Even Though Express Court Authorization Was Not Obtained Prior To The Rendition Of Such Services

A. The Court is Not Precluded in a Bankruptcy Proceeding from Exercising Equitable Powers.

Bankruptcy Courts have such equitable power as is necessary in aid of their bankruptcy jurisdiction, the exercise of that power being limited only insofar as it would be inconsistent with the Bankruptcy Act. *Young* v. *Higbee Co.*, 324 U.S. 204 (1945); *In re Keystone Realty Holding Co.*, 117 F.2d 1003 (3rd Cir. 1941); *Sampsell* v. *Monell*, 162 F.2d 4 (9th Cir. 1947); *In re Swofford*, 112 F. Supp. 893 (D. Minn. 1952). Thus, it has long been recognized that the provisions of the Bankruptcy Act dealing with the awarding of attorney's fees are not exclusive and that, in appropriate circumstances, it is well within the powers of the Bankruptcy Court to make such awards as justice and equity might dictate. As was stated in *In re Swofford*:

> "The authority of the bankruptcy court to tax attorney's fees as costs, in the absence of statutory authorization, rests in its equitable jurisdiction . . . .
>
> "The failure of Congress to provide expressly for attorney's fees in the instant situation does not, of itself, render a court's use of the equitable doctrine inconsistent with the Act." 112 F. Supp. at 895.

One situation universally considered appropriate for the exercise of the equitable power to award attorney's fees is that in which an attorney has taken upon himself the protection of a fund or has created a fund in which others may share. *See* 6 *Moore's Federal Practice* ¶ 54.77 [2], at 1704-07 (2d ed. 1972); *see also Sprague* v. *Ticonic National Bank*, 307 U.S. 161 (1939). As Judge Pollack, citing *Sprague*, stated below: "Such allowances are to be made as part of the Court's authority to do equity in a particular situation." (92a)

The Trustee cites *Berry v. Root*, 148 F.2d 945 (5th Cir. 1945), for the proposition that *Sprague* is not controlling in bankruptcy. (App. Brief, p. 11) In that case the attorneys had been employed for the purpose of defeating a bankruptcy proceeding. The Fifth Circuit Court stated:

> "We find no precedent or authority for a court of bankruptcy *with no estate before it* to assess money contributions against creditors as a personal liability to pay attorneys employed by other creditors for defeating the bankruptcy proceedings." 148 F.2d at 948.

The facts in that case did not justify the application of the equitable principle stated in *Sprague*. This Court has specifically recognized that the equitable doctrine stated in *Sprague* is applicable in bankruptcy under appropriate circumstances. In *Guerin* v. *Weil, Gotshal & Manges*, 205 F.2d 302 (2d Cir. 1953), this Court stated:

> "Such an allowance is 'appropriate only in exceptional cases and for dominating reasons of justice' [citing *Sprague* v. *Ticonic National Bank, supra* (1939)] and we do not think that securing an adjudication in bankruptcy is sufficiently analogous to these cases to warrant an extension of the principle." 205 F.2d at 304.

Indeed, Bankruptcy Courts have recognized the principle and are uniformly of the opinion that, although the power

to award fees must be exercised sparingly in order to effectuate the Bankruptcy Act's policy of economy for the Estate, the exercise of that power is appropriate where "a tangible benefit has been conferred on the estate to the advantage of the creditors as a whole." *Saper* v. *John Viviane & Son, Inc.*, 258 F.2d 826, 828 (2d Cir. 1958).

B. The Courts have Created an Exception to the General Rule that the Fee of a Creditor's Attorney is Not to be Paid fom the Bankrupt Estate.

While we are aware of the general proposition, relied upon by the Trustee, that a creditor's attorney's fee is not to be paid from the Bankrupt Estate, the Courts have created a widely-recognized exception to that proposition, an exception the requirements of which are met by the instant situation. Thus, in situations in which (1) the Trustee has refused or neglected to act and (2) the creditor's attorney has conferred a tangible benefit on the Estate by acting in the Trustee's stead, compensation from the Estate will be allowed. *In re New York Investors, Inc.*, 130 F.2d 90 (2d Cir. 1942); *In re Otto-Johnson Mercantile Co.*, 48 F.2d 741, 742 (10th Cir. 1931); *In re Roadarmour*, 177 F. 379 (6th Cir. 1910); *In re Alta Vineyards Co.*, 87 F. Supp. 608 (S.D. Cal. 1949); *In re J. A. Rudy & Sons*, 30 F. Supp. 8 (W.D. Ky. 1939); *In re Cheney*, 300 F. 465 (D. Mass. 1924); *In re Little River Lumber Co.*, 101 F. 558 (W.D. Ark. 1900); *see also Collier on Bankruptcy*, ¶¶ 62.21 at 1553, 62.29 [2.2] at 1571-72, 62.29 [2.4] at 1577-78 (14th ed. 1972). Compensation will be denied to creditors (*i.e.*, their attorneys) only "when the trustee is functioning in their behalf." *In re Otto-Johnson Mercantile Co., supra*, at 742. In short, this exception to the general rule rewards those who have enhanced the Bankrupt Estate while assuring that principles of economy will not have been violated by payment for needless services.

(1) The Trustee has ignored this exception.

The Trustee chose to ignore this widely-recognized exception, relying instead upon cases which have no application to the facts presented by the case at bar.

Thus, in *In re Progress Lektro Shave Corporation,* 117 F.2d 602 (2d Cir. 1941), the services for which an allowance was sought were all rendered by the attorney for a debtor under Chapter 10, which was subsequently adjudicated a bankrupt. He continued to render services following bankruptcy. The allowance was denied simply because he had rendered services to the Trustee which should have been performed by the attorney for the Trustee if one had been appointed. There was no creation of a fund for the benefit of all creditors as a result of the attorney's efforts and, accordingly, there was no call for the application of the exception to the general rule.

Guerin v. *Weil, Gotshal & Manges,* 205 F.2d 302 (2d Cir. 1953) involved an application for allowances for payment of accountants and appraisers who had been retained in connection with establishing the insolvency of the bankrupt. Such allowances, which had been granted by the District Court, were disapproved by this Court because they were not specifically allowed by any provision of the Bankruptcy Act. The Court stated, however, that "the only authority for the allowance would be the equity practice of allowing costs in certain cases, *as where a fund in which others will share has been produced by these expenses.*" (Emphasis supplied) This Court then quoted the principle set forth in *Sprague* v. *Ticonic National Bank,* 307 U.S. 161, 167 (1939) that such an allowance is "appropriate only in exceptional cases and for dominating reasons of justice." The Court refused, however, to apply the principle in that case because it did not think that "securing an adjudication in bankruptcy is sufficiently analogous to these cases to warrant an extension of that principle." (205 F.2d at 304)

In re Siegel, 252 F. 197 (S.D.N.Y. 1918), also heavily relied upon by the Bankruptcy Judge, is correct in its

application of the general rule of disallowance, simply because its facts require no other result. Indeed, the opinion indicates a recognition of the equitable exception on which we rely:

> "An estate in the custody of a court is not in need of voluntary services; there is no room for the doctrine of salvage. It is *presumably* being cared for adequately. . . ." *Id.* at 198 (emphasis added)

Thus, when the presumption that the Estate is "being cared for adequately" is rebutted (*i.e.*, when it is shown that the trustee has neglected or refused to act), the general rule of disallowance does not apply. Accordingly, *Siegel* cannot be viewed as authority for denying the instant application, even though it was there assumed that counsel for the creditors' committee did, in some degree, benefit the Estate, since there was no finding that the receiver had ceased to function or would not have acccomplished the same result.

C. The Courts Recognize an Exception to the "Prior Approval" Rule When the Trustee Fails to Act in the Best Interests of the Bankrupt Estate.

In addition to his misplaced reliance upon the general rule denying compensation to a creditor's attorney from the Bankrupt Estate, the Trustee, citing this Court's decision in *Sartorius* v. *Bardo,* 95 F.2d 387 (2d Cir. 1938), relies upon another general prerequisite for the awarding of fees, *to wit,* the requirement that the Court's express permission must be obtained prior to the rendition of services for which a creditor's attorney expects compensation. Here again, however, the Trustee has ignored an equitable exception engrafted upon the general rule. As this Court stated in the *Sartorius* case itself:

> "[O]bviously *if a creditor successfully opposes a proposal of the trustee,* it is no answer to his demand for payment to say that the trustee was in charge; by hypothesis his intervention was necessary. Hence

> *the judge would not have been justified in denying this part of the petition, if any substantial advantage could be traced to the service.*" 92 F.2d at 390 (emphasis added).

And in *In re Paramount Publix Corporation,* 85 F.2d 588 (2d Cir. 1936), cited by this Court in *Sartorius,* the exception to the general rule was stated thusly:

> "If some other committee or person proposes to seek compensation out of the general assets, there should be an application to the court for recognition, *preferably in advance* of the rendition of services for which compensation is to be sought. It should show the need of separate representation, and there should be an allowance out of the general estate only where those recognized have performed substantial services 'in connection with the proceeding or plan.' We have used the words 'preferably in advance,' because there may be situations where . . . [persons] are acting in pending estates with the tacit approval of the court though without an order recognizing them made upon a formal application. *In such cases it might prove an unexpected hardship to require an order in advance of the rendition of services where separate representation is found to have been necessary for proper administration. . . .*" 85 F.2d at 591 (emphasis added).

In re Porto Rican American Tobacco Co., 117 F.2d 599 (2d Cir. 1941), is another of the cases cited by Counsel for the Trustee as requiring prior Court approval for services to be rendered. The decision is based upon the *Sartorius* case, discussed above, states the same general rule, and recognizes the same equitable exception. The factual situation was one in which the legal services for which compensation was sought were not beneficial to the Estate. It was this fact which was crucial to the decision rendered. There are several portions of the opinion in which reference is made to the requirement that the Estate receive some benefit. Thus, it was said:

> "[I]t is clear that . . . [stockholders' and creditors'] attorneys can be compensated from the estate only if their services contributed to the confirmation or defeat of a plan or were beneficial in the administration of the estate. . . . [C]ompensation from the estate was allowable to the attorney . . . only to the extent of benefits received by the estate from his services." *Id.* at 601.

One year after its decision in *In re Porto Rican American Tobacco Company,* this Court found justification for a relaxation of the prior approval rule in *In re New York Investors, Inc.,* 130 F.2d 90 (2d Cir. 1942), the essential facts of which, we submit, are on all fours with those in the instant case. In *New York Investors* the largest creditor of the Estate, without prior approval of the Court, appealed the District Court's award of compensation to the Trustee and his counsel and was successful in having the awards reduced. After expressly referring to their reaffirmation of the "prior approval" rule in *Porto Rican American Tobacco Company,* this Court nonetheless thought that the circumstances justified a relaxation of the rule, stating:

> "Where the creditor has not unnecessarily duplicated the efforts of others, and where his services are such as the trustees cannot reasonably have been expected to perform, little difficulty can arise from omitting the requirement. Since this is so, we think that considerable freedom in raising objections, for the benefit of the estate, to allowances which the trustees are unable or most unlikely to question, may wisely be accorded to interested creditors, and we will not here penalize the applicant for a departure from the better practice which appears not to have prejudiced the administration of the estate." 130 F.2d at 92.

The applicability of *New York Investors* to the present situation is manifest—(1) our efforts clearly did not dupli-

cate the efforts of others, and (2) our services were such as the Trustee could not reasonably have been expected to perform. The Trustee, his Counsel and Special Counsel, as a result of their strong support for the $1,600,000 settlement offer, and later for the $2,000,000 offer, both of which we and the Assistant U. S. Attorney opposed successfully, have, in effect, been our adversaries throughout our participation in this matter. The increase from $1,600,000 to $2,473,070.12 in the amount for which the antitrust case was settled would never have occurred if attorneys from our office, familiar with antitrust cases, had not devoted the time required to make a full study of the antitrust case and concluded that $1,600,000 was *not* an excellent settlement (paraphrasing the statement in Special Counsel's Affidavit in opposition to our joint application for a rehearing and reconsideration of the Referee's Order of September 29, 1970. (84a)). Accordingly, just as the conclusion was reached in *New York Investors* that "little difficulty can arise from omitting the requirement" of prior court approval for the services rendered, so the Court below reached the same conclusion in holding that attorney's fees and disbursements should be awarded to us.

The Trustee maintains that the exception to the "prior approval" rule (reflected in *New York Investors*) does not aid our position since the Court there relaxed the rule only because it was clear that Trustees will not take appeals from their own allowances. The Trustee's position, we submit, reflects a misunderstanding of the basis of the decision. The fact that Trustee's allowances were involved is significant only insofar as that fact tended to show that the Trustee would not continue to function on behalf of the Estate. In other words, the involvement of Trustees' allowances acted as circumstantial proof of the existence of a situation in which "the trustees cannot reasonably have been expected to perform." In the instant case, no such circumstantial proof is required; our factual situation is

clearly a situation in which the Trustee, having accepted the $1,600,000 settlement offer, subject to approval of the Referee, had no intention of pursuing a greater benefit to the Estate (*i.e.*, an increased settlement offer).

The court in *In re Ira Haupt & Co.*, 280 F. Supp. 341 (S.D.N.Y. 1967), summarized the "prior approval" rule when it stated:

> "If creditors undertake to do the trustee's job for him, they do it gratuitously (in the absence of court order *or the trustee's failure to act*)." *Id.* at 344 (emphasis added).

This summary statement by the Court demonstrates that the Trustee's reliance upon such cases as *In re Hydrocarbon Chemicals, Inc.*, 411 F.2d 203 (3d Cir. 1969); *In re Progress Lektro Shave Corporation*, 117 F.2d 602 (2d Cir. 1941); *In re Eureka Upholstering Co.*, 48 F.2d 95 (2d Cir. 1931); and *In re Owl Drug Co.*, 16 F. Supp. 139 (D. Nevada 1936), is misfounded. In none of these cases was there any indication that the Trustee had ceased to act on behalf of the Estate. This Court, in *In re Progress Lektro Shave* recognized the exception to disallowance of legal fees for services rendered, if the Trustee refuses to act (117 F.2d at 604). Similarly, in *In re Owl Drug Co.*, 16 F. Supp. at 150, it was said: "They [trustee's attorneys] protected the estate ably and conscientiously. The work done by the attorneys for the bankruptcy in aiding them in these matters was, therefore, not required of them." The Court's finding of fact called into play the general rule but, at the same time, recognized the exception.

Additionally the Trustee has relied upon General Order 44 and Rule 215(a) of the Rules of Bankruptcy Procedure as establishing a statutory requirement of prior Court approval. [Rule 215(a) is not intended to differ substantially from its predecessor, General Order 44. See Advisory Committee's Note, Rule 215(a), Rules of Bank-

ruptcy Procedure.] In his brief a portion of Rule 215(a) is set out as follows: "No attorney or accountant *for the trustee* or receiver shall be employed except upon order of the court. . . ." (App. Brief p. 7) (emphasis added). When, however, one reads the next sentence of Rule 215(a), "The order shall be made only upon application *of the trustee or receiver. . . .*," (emphasis added), it becomes clear that the Rule has no application to the present situation. Since the application for the court order is required to be made by the Trustee, the Rule obviously does not attempt to encompass a situation in which creditor's counsel must step in because the Trustee has ceased to act, or refuses to act, in the best interest of the Bankrupt Estate. Rather, the Rule contemplates a situation in which the Trustee desires to employ counsel to assist him.

In summary, it is amazing indeed that Counsel for the Trustee, who together with his Special Counsel so vehemently disputed the value of the evidence of provable damage which we introduced in seeking rejection of the $1,600,000 settlement offer, and who so vigorously opposed our efforts to obtain and sustain the resulting disapproval of that offer, now claims full credit together with Special Counsel for the final settlement of $2,473,070.12, more than 50% greater than the offer which they had described as "an excellent settlement", and of which they urged approval by the Bankruptcy Judge, and gives no credit to us for our services involving 1769 hours of time. (52a)

If it had not been for the zealous efforts of Winthrop, Stimson, and if the matter had been left to Special Counsel and Counsel for the Trustee, the unwarranted $1,600,000 settlement would have been consummated to the great detriment of the creditors who would have received nothing. It must be remembered that Trustee and his Counsel strenuously supported and urged approval by the Bankruptcy Judge of the first proposed settlement at $1,600,000. It was

only when Winthrop, Stimson, together with the Assistant United States Attorney, demonstrated the inadequacy of this settlement and that the Trustee and his Counsel were in error in their contention that proof of damages was weak, that the higher settlement was achieved. It was only after the Bankruptcy Court on reargument disapproved the settlement of $1,600,000 and Judge Lasker had denied their Petition for Review that the Trustee and his Counsel were spurred into making further efforts at settlement, based upon evidence and proof Winthrop, Stimson had unearthed and developed. In the unique circumstances of this case, the Court can best protect Bankrupt Estates by awarding allowances to attorneys for creditors whose efforts have resulted in a greatly increased offer of settlement, in the face of the lethargy and despite the opposition of the Trustee and his Counsel.

We submit that Judge Pollack's opinion in the Court below properly reflects the current state of the law. It dealt adequately with those equitable considerations which encourage proper administration of Bankrupt Estates through rewarding those whose diligence enhances the Estate after the Trustee has ceased to protect the Estate.

Conclusion

The decision and order of the Court below should be affirmed.

Respectfully submitted,

WINTHROP, STIMSON, PUTMAN & ROBERTS

By Terence H. Benbow

Terence H. Benbow
A Member of the Firm
Attorneys Pro Se, Appellees

VICTOR S. TRYGSTAD,
STEVEN A. BERGER,
Of Counsel
New York, New York
Dated: August 14, 1974

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

DANIEL G. McDERMOTT , being duly sworn, deposes and says that deponent is not a party to this proceeding, is over 18 years of age, employed by Winthrop, Stimson, Putnam & Roberts, attorneys pro se .

That on the 15th day of August , 1974 , deponent served the within Appellee's Brief (Two copies)

upon the attorney(s) listed below at the address(es) designated by said attorney(s) for that purpose by depositing a true copy of same enclosed in a postpaid properly addressed wrapper, in an official depository under the exclusive care and custody of the United States Post Office within the State of New York:

Joseph L. Alioto, Esq.
111 Sutter Street
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Daniel G. McDermott
DANIEL G. McDERMOTT

Sworn to before me this
15th day of August, 1974.

James C. McMahon Jr.
Notary Public

JAMES C. McMAHON, JR.
Notary Public, State of New York
No. 31-4509064
Qualified in New York County
Commission Expires March 30, 1975

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